BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In re: Review of the Retail Rates of Florida Power & Light Company	:	DOCKET NO. 001148-EI
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	:	Submitted for Filing:
	:	March 4, 2002

DIRECT TESTIMONY OF
THEODORE J. KURY ON BEHALF OF
PUBLIX SUPER MARKETS, INC.

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PUBLIX SUPER MARKETS, INC.

Q: PLEASE STATE YOUR NAME AND OCCUPATION.

A: My name is Theodore J. Kury and I am a Senior Economist with SVBK Consulting Group, Inc., a subsidiary of Alliant Energy Integrated Services, located at 37 N. Orange Ave, Suite 710, Orlando, Florida 32801.

Q: PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A: A detailed description of my education and experience is included in my resume attached as Exhibit No.___(TJK-2).

Q: ON WHOSE BEHALF ARE YOU SPONSORING THIS TESTIMONY?

A: I am sponsoring this testimony on behalf of Publix Super Markets, Inc. ("Publix").

Q: WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A: I was retained by Publix to review the financial analyses and associated rates of return and common equity capital sponsored by Mr. Paul Evanson, Mr. Moray Dewhurst, and Dr. William E. Avera for Florida Power & Light Company ("FPL" or "the Company"). In the event that I disagreed with their financial analyses and return proposals, I was charged to develop and present a more realistic return proposal.

In addition, I have some concerns regarding the increased storm damage accrual proposed by Mr. Steven Harris and the load forecast adjustments proposed by Dr. J. Stuart McMenamin. These are addressed at the end of my testimony.

RATE OF RETURN

Q: HAVE YOU HAD AN OPPORTUNITY TO REVIEW THE COMPANY'S FINANCIAL ANALYSES AND RETURN PROPOSALS?

A: Yes, I have. My analysis of FPL's filing has led me to conclude that the return proposal propounded by Mr. Evanson, Mr. Dewhurst, and Dr. Avera is excessive, and therefore inequitable. If granted in this proceeding, this rate of return would unfairly enrich FPL Group, Inc. ("FPL Group"), the parent and sole common equity holder of FPL, at the expense of the Florida customers. In keeping with my charge from Publix, I performed a market-based financial analysis that produced common equity cost estimates and fair rate of return recommendations that, in my judgement, more accurately reflect the current and prospective financial circumstances of FPL and the capital market.

Q: PLEASE IDENTIFY THE FOUR EXHIBITS THAT ACCOMPANY YOUR TESTIMONY.

A: I have prepared four exhibits, attached herein, numbered TJK-3 through TJK-6 to supplement my testimony. Exhibit No.___(TJK-3) shows FPL's proposed rate of return, Exhibit No.___(TJK-4) shows the results of my Discounted Cash Flow analysis, Exhibit No.___(TJK-5) is my proposed rate of return for FPL, and Exhibit No.___(TJK-6) is a comparison of modeled and actual FPL storm damage.

Q: WHAT CONCLUSIONS HAVE YOU DRAWN REGARDING THE RATE OF RETURN FOR FPL IN THIS CASE?

A: My recommended return on common equity for FPL is 9.92%, resulting in an overall rate of return

of 7.72%, as shown in Exhibit No.___(TJK-5). The effect of this rate of return is approximately $175 million to the FPL retail customer.

Q: WHAT CONSTITUTES A COMPANY'S RATE OF RETURN?

A: The rate of return is also known as a weighted average cost of capital. This is the average cost of long-term debt, short-term debt, accumulated deferred income taxes, other deferred balances, preferred stock, and common equity weighted by the percentage of each component in the company's capital structure.

Q: WHAT IS FPL'S CAPITAL STRUCTURE?

A: FPL's capital structure, shown in Exhibit No.___(TJK-3), was reported in Schedule D-1 of the Minimum Filing Requirements filed by FPL in this docket, as revised on November 9, 2001. This reflects FPL's 13 month average capital structure for the test year ended 12/31/2002.

Q: WHAT IS THE COST OF FPL'S LONG TERM DEBT?

A: FPL has claimed that its cost of long-term debt is 6.25%, shown in Exhibit No.___(TJK-3). This is the average annualized contractual cost of all outstanding long-term debt contained in the capital structure. It includes annual interest charges and amortization of premiums, discounts, and expenses, expressed as a percentage. However, the Company's claimed cost of long term debt is based on a cost of 7.37% for $250 million of long-term debt that was estimated to be issued in 2001 and another $250 million of long-term debt to be issued in 2002. In its response to Staff's Seventh Set of Interrogatories, Interrogatory No. 249, the Company demonstrates that this cost projection is based on the 30 Year Treasury Bond Yield from the June 1, 2001 Blue Chip Financial Forecast

plus a credit spread of 1.67% based on an interpolation between Aaa and Baa bond ratings. If the 30 Year Treasury Bond Yield is updated to the closing at February 25, 2002 of 5.37%, the cost of the new debt falls to 7.04%. Applying this cost of 7.04% to FPL's Schedule D results in a revised cost of long-term debt of 6.22%. This revised cost of long-term debt is shown in Exhibit No.___(TJK-5).

Q: WHAT IS THE COST OF FPL'S SHORT TERM DEBT?

A: FPL's cost of short-term debt is 4.92%, shown in Exhibit No.___(TJK-3). This is the average annualized contractual cost of all outstanding short-term debt contained in the capital structure. It includes annual interest charges and amortization of premiums, discounts, and expenses, expressed as a percentage.

Q: WHAT IS THE COST OF FPL'S PREFERRED STOCK?

A: FPL's cost of preferred stock is 4.51%, shown in Exhibit No.___(TJK-3). This is the average annualized contractual cost of all outstanding preferred stock contained in the capital structure, expressed as a percentage.

Q: WHAT IS THE COST OF FPL'S COMMON EQUITY?

A: FPL's witness, Dr.Avera, proposes a cost of common equity of 12.85%, which is adjusted upward by 30 basis points to 13.15% based on the recommendation of FPL witness Dewhurst. As I explain later in my testimony, this proposed cost of equity is excessive due to the improper application of a growth rate, the improper inclusion of a flotation cost adjustment, and the improper inclusion of a reward mechanism. I am proposing a cost of common equity of 9.92%, as shown in

Exhibit No.___(TJK-5). This represents a fair and reasonable rate of return on FPL's common equity.

Q: WHAT CONSTITUTES A FAIR AND REASONABLE RATE OF RETURN ON COMMON EQUITY?

A: The concept of a fair and reasonable rate of return on common equity is a relatively straightforward deduction from modern economic and finance theory. It is based on the economic principle of risk-adjusted, investor opportunity costs. At this conceptual level, the fair rate of return is normally not the subject of great dispute. By contrast, its estimation in regulatory proceedings is typically controversial.

Fortunately, there are sensible and useful economic and financial guidelines or standards established by the Supreme Court in the Bluefield and Hope opinions which may be employed in the estimation of this all-important common equity cost measure.[1] These Court-established economic guidelines serve as the underpinnings of both my financial analysis and final estimates of the fair and reasonable rate of return on FPL's common equity.

In the Hope opinion, for example, the Court provided the basic standards and tests of a fair rate of return on equity as:

1. ... the return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks.

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[1] Bluefield Water Works and Improvement Company v. Public Service Commission of West Virginia, 262 U.S. 879, 893 (1923). Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944).

2. The return, moreover, should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and attract capital.

The Court has thus established two standards -- a standard of risk-adjusted, comparable return to investors and a standard of capital attraction -- as essential characteristics of a fair rate of return on common equity.

These standards are precise analogues of the generally recognized operational principles of a free market, viz., that a firm, in order to maintain its ability to attract capital at reasonable rates, must be able to earn a rate of return on common equity which is at least equal to the risk-adjusted opportunity costs of investors in the market. The risk-adjusted opportunity costs of investors in the market, in turn, may be defined as the rate that investors could earn by placing their capital in other enterprises entailing comparable measures of risk exposure. In terms of regulatory principles, the Court-established standards of regulation mandate that regulated firms be granted the opportunity to earn a rate of return on common equity which is equal to the risk-adjusted opportunity costs of investors in the market.

The Court-established regulatory concept of a fair rate of return on common equity incorporates considerations of both equity and economic efficiency. The rate will be equitable to investors in that it just compensates them for the risk to which they are exposed in purchasing and/or holding the common stock of a specific firm. At the same time, that rate will be equitable to customers in that it is the minimum supply price required to assure a continuing supply of equity capital to the company. The fair rate of return thus achieves the primary objective of regulation -- a balancing of the

competing interests of customers and stockholders. The fair rate of return, being the market-established minimum supply price of equity capital, is that rate which is both necessary and sufficient to maintain the financial integrity and capital attracting ability of the firm.

A rate of return greater than that which is necessary and sufficient would serve to both enrich investors at the expense of customers and to encourage an excessive rate of investment spending, resulting in a misallocation of resources coupled with a larger-than-necessary future revenue requirement and level of rates. A rate of return that is less than sufficient would result in inadequate profits, thus penalizing investors and inhibiting the firm's ability to meet its public service responsibility. The fair rate of return, therefore, is not only equitable, but is also economically efficient in that it is the level that is sufficient to guarantee the firm's access to necessary capital, while assuring its ability to serve customers at the market-established minimum, necessary cost.

Q: WOULD YOU EXPLAIN THE METHOD YOU USE TO DEVELOP YOUR RATE OF RETURN RECOMMENDATION?

A: My primary analysis is based upon the traditional specifications of the Two-Stage Discounted Cash Flow ("DCF") stock valuation model.

Q: PLEASE EXPLAIN WHY YOU PLACE PRIMARY RELIANCE UPON THE DCF MODEL.

A: The DCF method is analytically sound in that it is: rooted in observable economic behavior; relatively explicit in terms of method, assumptions, data requirements, and calculations; and, when reasonably applied, produces estimates consistent with the regulatory standards established in the Bluefield and Hope decisions. Moreover, because of its explicit nature, it is a method by which the

results may be tested or replicated.

The logic of the DCF model derives from the sensible and widely applied notion that the value or market price of any asset is a direct reflection of the prospective holder's perception of the ability of that asset to yield a flow of services or income over time. This concept is illustrated in the equation below:

$$P_t = \frac{D_t}{(1+r)} + \frac{D_t(1+g_{t+1})}{(1+r)^2} + ..+ \frac{D_t(1+g_{t+n})+P_{t+n}}{(1+r)^{n+1}}$$

Where:

P_t = Market price at time t;

D_t = Expected dividend payment at time t;

r = Investors' discount rate;

g_t = Investors' expected dividend growth rate at time t.

The discount rate represents investors' risk-adjusted opportunity costs and is equal to the investor-perceived rate of return on comparable risk alternatives available in the market. This variable (r) is frequently referred to as the investor capitalization rate, i.e., the rate at which investors capitalize a prospective flow of income payments.

This stock valuation model simply says that, given the market price of a stock at a point in time, investors will make buy-sell decisions with respect to that particular stock, and thus alter its price, by comparing its potential to yield a rate of return (an expected flow of dividends and capital gains)

with the rate of return currently being earned on comparable risk stocks. If the rate of return on the stock of a given company is either greater or less than is being earned on comparable risk stocks, then investors will alter their buy-sell decisions in such a way as to change the market price of the stock so as to equalize rates of return among assets with similar risks.

If it is assumed that the market evaluates the income potential of a stock over a long period of time and that the prospective growth rate of dividends can be reasonably described by a compound rate, then the DCF equation above can be simplified mathematically into the more familiar DCF equation:

$$P_i = \frac{D_i}{r - g}$$

This equation simply says that the observed market price of a share of stock is equal to the current nominal dividend divided by the difference between the investor capitalization rate and the rate of growth expected by investors.

Consider, for example, a common stock which is currently paying a $2.00 per annum dividend (D) which is expected to grow in the foreseeable future at a 3.0 percent annual compound rate (g) for a company which has an investors' risk-adjusted opportunity cost or capitalization rate (r) of 11.0 percent. Under these circumstances, the stock in question would necessarily have an equilibrium, or market-clearing, price (P) of $25.00 per share. If the actual market price were either higher or lower than $25.00 per share, supply and demand forces would operate to drive the price to the

$25.00 figure. Given the dividend yield and expected rate of growth, this is the only price which allows investors to receive a rate of return equal to the 11.0 percent posited as currently available on comparable risk alternatives in the market, i.e., a rate of return which is just equal to investors' risk-adjusted opportunity costs.

The use of this DCF stock valuation model for estimating the market-determined cost of common equity (r) is based on the presumption that meaningful measures of P, D, and g can be estimated. If such measures can be established, then the cost of common equity can be estimated by solving for r

$$r = \frac{D_t}{P_t} + g$$

in the following equation:

In order to allow for the real world fact that dividends are most commonly paid on a quarterly

$$r = \frac{D_t(1+0.5g)}{P_t} + g$$

basis, the above equation can be respecified as:

Q: ARE FPL'S DIVIDEND YIELDS AND GROWTH FACTORS READILY AVAILABLE?

A: No, FPL's common equity is not publicly traded. All of the common equity of FPL is held by its parent company, FPL Group. FPL-specific information is thus not available. The theory of efficient markets relies on a large number of buyers and sellers and thousands of transactions to determine

the fair market value of a commodity. These conditions are not met in the case of FPL's common equity.

Q: HOW WOULD THE COST OF FPL'S COMMON EQUITY BE DETERMINED?

A: FPL is a wholly-owned subsidiary of FPL Group, and, as such, has no market presence for its common equity. All FPL common equity comes through the parent company, FPL Group. This means that the cost of common equity capital to FPL can be no greater than the cost of common equity capital to FPL Group. It follows, then, that in this proceeding it is appropriate for the analysis to focus on FPL Group, to estimate the cost of common equity capital on FPL Group, and to impute this equity cost rate to FPL.

Q: HOW CAN THE COST OF FPL GROUP'S COMMON EQUITY BE DETERMINED WITH A MARKET-BASED METHODOLOGY?

A: The DCF method can be applied to FPL Group and a group of utilities that are similar to FPL Group. Because investors should require the same return from companies with similar risks, the required return on a group of comparable companies can be used to infer the required return on FPL Group.

Q: PLEASE EXPLAIN YOUR COMPARABLE GROUP DCF RESULTS.

A: I prepared DCF analyses using the data available in the Value Line Investment Survey ("Value Line"). Value Line rates the relative Safety and Financial Strength for each company it evaluates. FPL Group is rated 2 for Safety and A for Financial Strength. For my comparable group, I chose companies within the Electric Utility industry group that are electric-only utilities, and are rated

either 2 for Safety or A for Financial Strength. There are 7 such companies.

For the dividend yield component of the DCF model, I used the average dividend yield for the previous three months ending January 31, 2001, the most recent month as of the date of writing. For the growth component, I implemented a "two-stage" DCF model, consisting of the average of a short-term and a long-term growth rate.

For the short-term growth rate, I used the average of Value Line's three-to-five year projected growth rates of earnings and dividends. However, an assumption of the DCF model is that investors have a long-term investment horizon, and these growth estimates are only valid for the short term. It is reasonable to assume that investors will base long-term expectations on the rate at which the economy is expected to grow. For a long-term growth rate, therefore, I have used the long-term nominal Gross Domestic Product forecast of 6.1% from the 2002 Annual Energy Outlook published by the Department of Energy's Energy Information Administration. I then averaged these short-term and long-term growth rates to determine the growth rate used in the DCF model. I performed the DCF calculation for each company in the comparable group for FPL Group, and averaged these DCF results to determine a fair rate of return on FPL Group's common equity.

Q: WHY DO YOU RELY ON VALUE LINE'S DATA AND RANKINGS?

A: When dealing with the expectations of investors, it is best to get information from a source on which investors rely. Value Line is a widely disseminated investment advisory letter, available in public libraries across the country. Value Line's Safety and Financial Strength ratings encompass a broad spectrum of financial data, leading to Value Line's assessment of a company's business and

financial risk. Further, while interest coverage ratios, common equity ratios, and other traditional measures of financial strength could be individually examined, the Value Line ratings provide a non-biased opinion based on significant market research.

Q: WHAT ARE THE RESULTS OF YOUR COMPARABLE GROUP ANALYSIS OF DCF MODELS?

A: The average 3-month dividend yield for FPL Group through January 31, 2001 was 4.05%. The average of the Value Line Dividend and Earnings growth rates is 4.00%. When averaged with the long-term growth rate, this results in a Two-Stage growth rate of 5.05%. Applying the DCF equation with these inputs results in a common equity return of 9.20%. Applying the DCF equation to the other members of the comparable group and averaging these returns results in an average return on common equity of 9.92%. These calculations are shown in the attached Exhibit No.___(TJK-4).

Q: HOW DO YOU RECONCILE YOUR RECOMMENDED RETURN ON COMMON EQUITY WITH DR. AVERA'S RECOMMENDED RETURN OF 13.15%?

A: Dr. Avera's analysis differs from mine on three major points. First, Dr. Avera uses only short-term growth rates, rather than a growth rate recognizing both long and short-term trends. Second, Dr. Avera employs a flotation cost adjustment to his cost of common equity. Third, Dr. Avera employs a reward mechanism of 30 basis points to his cost of common equity.

Q: IS THE GROWTH RATE USED BY DR. AVERA REASONABLE?

A: No. Dr. Avera has used earnings estimates published by I/B/E/S, Value Line, Zacks Investment

Research, and First Call Corporation in his DCF model. These growth rates are analysts' projections of short-term earnings growth only, typically the next three to five years. The DCF model assumes a constant, infinite growth rate, and it is inappropriate to assume that investors expect such a short-term rate to continue indefinitely. This is why I chose a two-stage growth rate, a combination of a short-term rate and a long-term rate. This two-stage growth rate better reflects investor expectations over the time horizon of the DCF model. In addition, Dr. Avera has used growth rates based on the product of an earnings retention ratio and an earned rate of return on book equity, or a so-called "b x r" growth rate. This growth rate is inappropriate for use in a DCF model because the DCF model itself is used to derive the rate of return on equity, yet an assumption of earned rate of return must be made in order to determine a growth rate.

Q: WHAT ARE FLOTATION COSTS?

A: Flotation costs are the costs associated with new issues of debt or equity. They include expenses such as underwriting expenses, the printing of stock certificates or bonds, and any associated administrative expenses. Dr. Avera has included a flotation cost adjustment of 25 basis points.

Q: DO YOU AGREE WITH DR.AVERA'S FLOTATION COST ADJUSTMENT TO HIS COST OF COMMON EQUITY?

A: No, I do not. FPL has not announced its intention to issue any common equity in the future, so this adjustment is designed to recover costs from the Florida customer that FPL has no intention of incurring.

Q: WHAT IS THE EFFECT OF THIS FLOTATION COST ADJUSTMENT ON FPL'S RETAIL CUSTOMERS?

A: If the 25 basis points are multiplied by FPL's equity ratio of 55.56%, the resulting impact on FPL's overall weighted average cost of capital is an increase of 13.89 basis points. Multiplied by FPL's rate base of $9.873 billion, this flotation cost adjustment increases FPL's revenue requirement by approximately $13.7 million after taxes and approximately $22 million before taxes. The Florida customer will thus be paying $22 million per year to recover costs that do not exist.

Even if the Commission decides that a flotation cost adjustment is necessary, the adjustment should not be applied to the portion of common equity financed by retained earnings. There are no costs of underwriting, printing stock certificates, or program administration associated with retained earnings.

Q: WHAT REWARD PROVISION HAS MR. DEWHURST PROPOSED?

A: Mr. Dewhurst has proposed a 30 basis point increase to the return on equity proposed by Dr. Avera.

Q: WHY HAS MR. DEWHURST PROPOSED THIS REWARD MECHANISM?

A: Mr. Dewhurst contends that FPL should be rewarded for "the superior efforts of the Company's management". (Dewhurst p. 3) As evidence of this superior effort he cites the return of excess revenues to customers and an increase in operating efficiency.

Q: CAN THE RETURN OF EXCESS REVENUES BE ATTRIBUTED TO SUPERIOR EFFORTS OF THE COMPANY'S MANAGEMENT?

A: No, it cannot. The revenues earned by FPL are directly attributable to its level of sales. FPL witness Waters has explained that "FPL develops econometric models to explain and predict the level of energy sales. Explanatory factors, such as the weather, the price of electricity, the economic conditions in Florida, the number of customers and seasonal factors are used to develop the forecast of energy sales." (Waters p. 56) Mr. Waters does not mention any variables that relate to the performance of management. Further, FPL witness McMenamin details the independent variables used in the load factor regressions on pages 3 and 4 of his testimony and states that "The fit for the Net Energy model is extremely strong (R square = .98, Mean Absolute Percentage Error = 1.7%)". (McMenamin p. 6) This means that these factors, outside of the influence of FPL management, explain 98% of the variation in Net Energy. Even if we attribute some portion of the unexplained variation to "management skill", it is at most 2%.

Q: CAN ANY DECREASE IN FPL COSTS AND IMPROVEMENT IN CUSTOMER SERVICE BY ATTRIBUTED TO SUPERIOR EFFORTS OF THE COMPANY'S MANAGEMENT?

A: Apparently not entirely. FPL witness Dewhurst states that, "Over the past several years, with the benefit of steady, predictable growth in customers and usage, and a stable planning environment, the Company has been able to keep costs relatively low while simultaneously improving customer service." (Dewhurst p. 2) Therefore, even FPL's own witnesses admit that these objectives are influenced by economic and regulatory factors beyond the control of FPL management.

Q: DO YOU AGREE WITH THE REWARD MECHANISM PROPOSED BY MR. DEWHURST?

A: No, I do not. He seeks to encourage the Company to maximize its cost cutting and other efficiency improvements, but the Company's return on equity may increase for many reasons, many out of its control. The Company's rate of return may increase if sales increase due to extreme weather, if customers act to shift load to off peak hours, or if the Company were to implement imprudent reductions in operation and maintenance costs. The Company has done nothing positive in any of these instances, yet would be rewarded.

Further, a DCF analysis such as Dr. Avera's is a mathematical attempt to determine a fair rate of return for FPL, that is, a risk-adjusted opportunity cost of equity capital. Any increase above and beyond that rate of return is, by definition, unfair to the Florida customer.

Q: DO YOU BELIEVE A REWARD MECHANISM IS APPROPRIATE?

A: No. My testimony proposes a fair rate of return on common equity for FPL. In return for this fair rate of return, FPL is obligated to provide reliable electric service at the least cost. The only reward that my client receives for keeping their frozen food frozen is continued operation. FPL is not entitled to any additional reward for doing its job properly.

Q: DO YOU HAVE OTHER CONCERNS WITH THE REWARD MECHANISM?

A: Yes. I am concerned with the Company's desire to be rewarded without accountability. When questioned about a system that would provide for penalties in the case of frequent outages, FPL witness Armando J. Olivera states that "Implementing a new regulatory regime that penalizes utilities

for "frequent outages" raises a host of policy issues that are more appropriately addressed in an industry-wide rulemaking. Such issues include: whether the mechanism should be based on a company's overall reliability versus isolated incidents, whether benchmarks or standards are required to assure specific levels of reliability, whether the approach should be symmetrical in operation (i.e. also authorizing surcharges for no or "less than frequent" outages), whether the costs of implementing such a program exceed the benefits, and whether such a program would expose the utilities and the Commission to a tidal wave of new complaints and causes of action." (Olivera p. 9) Mr. Olivera's issues just as appropriately apply to the implementation of a reward mechanism.

Q: MR. DEWHURST CITES SEVERAL RISK FACTORS SUPPORTING A HIGHER ROE. DO YOU AGREE THAT THESE RISK FACTORS REQUIRE A HIGHER ROE?

A: No. The risk factors cited by Mr. Dewhurst: general economic uncertainty and growth of service territory, customer base, volatile economy, nuclear generation, and geographic position, are all accounted for within the Financial Strength and Safety ratings of Value Line. While the some of the companies within my comparable group may have different specific risk factors than FPL, Value Line has rated them as having similar degrees of risk. Further, over 40% of FPL's revenues go through adjustment clauses that substantially lower risks to investors as compared to companies with lower portions of their revenues "guaranteed".

Q: DO YOU BELIEVE THAT YOUR RECOMMENDED RATE OF RETURN IS EQUITABLE FOR FPL AND THE FLORIDA CUSTOMER?

A: Yes, I do. My recommended rate of return is fair to FPL and to the Florida customers.

STORM DAMAGE ACCRUAL

Q: WHAT ARE YOUR CONCERNS WITH THE PROPOSED INCREASE IN THE STORM DAMAGE ACCRUAL?

A: I am concerned that the storm damage model developed by Mr. Harris overstates the damage that could be reasonably expected for FPL's transmission and distribution assets. At more reasonable damage expectations, the increase in the storm damage accrual proposed by Mr. Dewhurst will cause the storm damage fund to continue to grow to levels beyond what is necessary to maintain system integrity.

Q: WHY DO YOU THINK THAT MR. HARRIS' MODEL OVERSTATES EXPECTED STORM DAMAGE?

A: I have examined the Table 6-1 of the Storm Reserve Loss Analysis, Document SPH-1, Page 23 of 44 ,in which Mr. Harris' compares his model's storm damage estimates for six storms to the actual losses sustained by FPL. Table 6-1 shows that Mr. Harris' model has predicted actual storm losses within 1%, with nominal storm costs escalated 4% per year to reflect 1999 dollars. Mr. Harris states that he has used 4% despite his assertion that "Recent inflationary cost increases for new transmission and distribution assets have increased at 1% to 3.5% per year over the past decade." (Harris p. 6) However, as shown in Exhibit No.___(TJK-6), Mr. Harris did not escalate historical

costs at 4% in Table 6-1. He has, without explanation, escalated historical costs at 7.55% for three storms and 6.44% for Andrew. If actual costs are escalated at the 4% that Mr. Harris claims to use in his table, his model has overestimated FPL actual losses by 13.66%. Further, if escalators based on the Handy-Whitman Index of Utility Construction Costs for the Southeast United States ("Handy-Whitman") are applied, his model has overestimated FPL actual losses by over 25%. These calculations are shown on Exhibit No.___(TJK-6).

I have some additional concerns with the table on Exhibit SPH-3, Page 8 of 12, which lists the Aggregate Damage Exceedance Probabilities for his model. Hurricane Andrew was the most costly Atlantic coast hurricane in the past 100 years. If the Handy-Whitman index is used to express the costs incurred by FPL as a result of Hurricane Andrew in 2001 dollars, the cost is approximately $342 million. An examination of Mr. Harris' table on Page 8 of 12 shows that the probability of exceeding this damage level, within his model, in any one year is 4.069%. In other words, Mr. Harris' model predicts a storm of Andrew's damage capability *or greater* once every 25 years. This prediction is a gross overstatement of what has been historically observed.

Q: DO YOU HAVE A RECOMMENDATION REGARDING THE LEVEL OF FPL'S STORM DAMAGE ACCRUAL?

A: Yes. I believe that the current level of storm damage accrual is sufficient.

Q: WHY DO YOU BELIEVE THAT THE CURRENT LEVEL OF STORM DAMAGE ACCRUAL IS SUFFICIENT?

A: In its response to Publix First Set of Interrogatories, Interrogatory No. 4, FPL provided a detail of

annual Storm and Property Insurance Reserve activity since 1994. Since 1996, contributions to the reserve have totaled $121.8 million, and fund earnings have totaled approximately $63 million. In the same time period, storm costs charged to the reserve have totaled approximately $145 million, allowing the reserve to grow by $58 million (after a deposit of insurance proceeds).

In the testimony of FPL witness Dewhurst, he argues that the current accrual level is insufficient and states that "the reserve balance has actually declined with the current funding level of $20.3 million per year, despite a period of relatively low losses from actual storms, relative to what statistically could have been expected". (Dewhurst p. 31) Data available from the National Hurricane Center shows that for the period 1900-1996, 57 hurricanes have directly hit the entire state of Florida, an average of 0.58 storms per year. In the five years since, FPL service territory alone has been damaged by three hurricanes that directly hit the state of Florida (Georges, Irene, and Gabrielle), and another that made landfall in North Carolina (Floyd). This certainly appears to be average or even above average storm activity for the past five years, and yet the level of the reserve has increased nearly $13 million during this time.

In addition, in its response to Staff's Seventh Set of Interrogatories, Interrogatory No. 247, FPL states that it has had T&D insurance on poles and wires since 1999, with a deductible of $50 million. In his deposition on February 28, 2002, Mr. Dewhurst indicated that the policy covers 16% of losses above the deductible; therefore, FPL does have some additional protection against storm damage. Other options such as the extension of FPL's line of credit or prospective cost recovery proceedings are available in the event of another "Andrew"-type catastrophe.

Q: WHAT IS THE EFFECT OF YOUR RECOMMENDATION ON THE FLORIDA CUSTOMER?

A: My recommendation to maintain the storm damage accrual at its current level will reduce the revenue requirement to the Florida customer by approximately $29.8 million.

LOAD FORECAST ADJUSTMENTS

Q: HAS FPL MADE ANY ADJUSTMENTS TO ITS LOAD FORECAST?

A: Yes. Dr. J. Stuart McMenamin has testified that FPL has changed four assumptions in their load forecast in the wake of the attacks on September 11, 2001. In its revised load forecast, FPL has assumed lower customer growth, lower real per capita income, has removed added telecom load, and has removed an error adjustment term.

Q: DO YOU BELIEVE THAT FPL SHOULD HAVE MADE THESE ADJUSTMENTS TO ITS LOAD FORECAST?

A: No, I do not. FPL should not be allowed to selectively change only such assumptions that will skew its load forecast downward. If FPL believed that it was necessary to revise the assumptions in its load forecast, then it should revise all of the assumptions, and not just the assumptions that will decrease the forecast. Dr. McMenamin has stated in his testimony that the elasticity of real per capita income is positive; therefore, FPL knew that by revising its estimate downward, it would be decreasing its load forecast. Dr. McMenamin justifies the removal of the telecom load by stating that the Internet bubble has just now burst, when in fact technology stocks have been in a steep decline for over a year. And finally, FPL's intercept adjustment is simply an ad-hoc shifting of the

regression line downward without any statistical justification.

FPL has essentially allowed a preordained conclusion to determine the assumptions, rather than allow a complete, consistent set of assumptions to determine the conclusion.

Q: DO YOU HAVE A RECOMMENDATION AS TO THE PROPER LOAD FORECAST FOR FPL?

A: Yes. I believe that the proper load forecast for FPL should be based on a complete, consistent set of assumptions, such as the original load forecast.

Q: DOES THIS CONCLUDE YOUR TESTIMONY AT THIS TIME?

A: Yes, it does.

THEODORE J. (TED) KURY

Position Senior Economist, SVBK Consulting Group

Education

B. A. in Economics
State University of New York at Buffalo
Buffalo, New York

M.A. in Economics
State University of New York at Buffalo
Buffalo, New York

[45 credit hours post MA graduate work]

Professional and Business History

SVBK CONSULTING GROUP	1996 - Present
University of Central Florida Adjunct Faculty in the School of Business Administration, Department of Economics	1997 - Present
University of Central Florida	1996
State University of New York at Buffalo	1993 - 1995

Professional Experience

Mr. Kury is a Senior Economist in the Firm and has been extensively involved in assisting clients with electric industry restructuring issues. He has presented expert testimony pertaining to issues relating to stranded cost calculation and recovery, market pricing, and public policy concerns before the New Hampshire Public Utilities Commission and has assisted in the preparation of expert testimony on restructuring issues before the Federal Energy Regulatory Commission and various state commissions. He has participated in technical conferences and generic proceedings held to set policy issues associated with restructuring. Mr. Kury has been instrumental in developing stranded cost recovery alternatives for mediation and settlement negotiation. Mr. Kury has been involved with helping clients value electric generation assets and analyze alternate rate structures, as traditional regulation gives way to the advent of competition.

Mr. Kury has assisted clients with resource management issues. He has been instrumental in developing chronological generation computer models and market price forecasting to explore the effects of a competitive electric market on the way a utility makes its decisions. He has also aided utilities in expanding their business options in the marketing of capacity and energy.

Mr. Kury has been involved in a variety of electric, water and wastewater utility projects. He has represented clients in rate proceedings, including review of company filings, and assistance in the development of testimony, cross-examination of witnesses, and legal briefs and pleadings. Mr. Kury has prepared retail rate and cost-of-service studies, including the preparation and development of allocated cost-of-service computer models, determination of net revenue requirements, forecasting and development of billing determinants, rate design, rate comparisons, and the development of rate/tariff sheets. In addition, Mr. Kury has been responsible for developing computerized models for numerous financial and economic analyses for a variety of projects nationwide.

Mr. Kury has been involved in the development of consulting engineers' or financial feasibility reports for use in revenue bond official statements supporting the issuance of utility revenue bonds. These letter reports include historical and projected operating results, debt service coverage calculations, water use projections, and rate determination.

Mr. Kury also teaches economic theory at the University of Central Florida, and is a frequent speaker there on transitions from a regulated monopoly to a competitive industry.

Prior to joining SVBK, Mr. Kury was employed as an instructor at the State University of New York at Buffalo where he taught micro- and macro-economics. He has also worked for the University of Central Florida under a research grant in the field of industrial organization and technological change.

Papers and Publications

"The Use of Voluntary Export Restrictions as a Weapon in International Trade" - Presented for Dr. Winston Chang's graduate seminar on international trade.

"A Probit Analysis of Rehiring Decisions in Major League Baseball" - Presented for Dr. In-Moo Kim's graduate seminar on the econometrics of limited-dependent variables.

Publix Super Markets
Exhibit No.___(TJK-3)
Filed FPL Cost of Capital - 13 Month Average (in $000)

	FPSC Adjusted Retail	Ratio	Cost Rate	Weighted Cost
Common Equity	5,505,315	55.56%	11.83%	6.57%
Preferred Stock	227,170	2.29%	6.59%	0.15%
Long-Term Debt	2,808,533	28.34%	6.25%	1.77%
Short-Term Debt	52,463	0.53%	4.20%	0.02%
Customer Deposits	268,464	2.71%	6.02%	0.16%
Investment Tax Credit				
Deferred Tax Credit - Weighted Cost	130,531	1.32%	9.86%	0.13%
Deferred Income Taxes	916,379	9.25%	0.00%	0.00%
Total Capital Structure	9,908,855			8.81%

Notes:

[1]The weighted cost of the deferred investment tax credit is the weighted average cost of Common Equity, Preferred Stock and Long Term Debt as shown:

Common Equity	5,505,315	64.46%	11.83%	7.63%
Preferred Stock	227,170	2.66%	6.59%	0.18%
Long-Term Debt	2,808,533	32.88%	6.25%	2.06%
Total				9.86%

Publix Super Markets
Exhibit No.___(TJK-4)
DCF Results

Company	Ticker Symbol	Value Line Safety	Value Line Financial Strength	3 Month Dividend Yield	Value Line Earnings	Value Line Dividends	ST Growth Rate[1]	LT AEO Growth Rate	2 Stage Growth Rate[2]	DCF[3]
FPL Group	FPL	2	A	4.05%	4.50%	3.50%	4.00%	6.10%	5.05%	9.20%
Black Hills Corp	BKH	2	A	3.65%	11.00%	3.50%	7.25%	6.10%	6.68%	10.45%
CLECO	CNL	2	B++	4.25%	8.00%	2.50%	5.25%	6.10%	5.68%	10.04%
Empire District	EDE	2	B++	6.15%	4.50%	0.00%	2.25%	6.10%	4.18%	10.46%
Otter Tail	OTTR	2	B++	3.63%	5.50%	2.00%	3.75%	6.10%	4.93%	8.64%
Southern Company	SO	2	B++	5.56%	6.50%	2.50%	4.50%	6.10%	5.30%	11.01%
UIL Holdings	UIL	2	B++	5.70%	3.00%	0.00%	1.50%	6.10%	3.80%	9.61%
Average										**9.92%**

Notes:

[1]Average of Value Line Earnings and Dividends Growth Rates

[2]Average of Short Term and Long Term Growth Rate

[3]Dividend Yield multiplied by 1 plus 0.5 times the Growth Rate plus the Growth Rate

Publix Super Markets
Exhibit No.___(TJK-5)
Proposed FPL Cost of Capital - 13 Month Average (in $000)

	FPSC Adjusted Retail	Ratio	Cost Rate	Weighted Cost
Common Equity	5,505,315	55.56%	9.92%	5.51%
Preferred Stock	227,170	2.29%	6.59%	0.15%
Long-Term Debt	2,808,533	28.34%	6.22%	1.76%
Short-Term Debt	52,463	0.53%	4.20%	0.02%
Customer Deposits	268,464	2.71%	6.02%	0.16%
Investment Tax Credit				
Deferred Tax Credit - Weighted Cost	130,531	1.32%	8.61%	0.11%
Deferred Income Taxes	916,379	9.25%	0.00%	0.00%
Total Capital Structure	9,908,855			7.72%

Notes:

[1]The weighted cost of the deferred investment tax credit is the weighted average cost of Common Equity, Preferred Stock and Long Term Debt as shown:

Common Equity	5,505,315	64.46%	9.92%	6.39%
Preferred Stock	227,170	2.66%	6.59%	0.18%
Long-Term Debt	2,808,533	32.88%	6.22%	2.05%
Total				8.61%

Publix Super Markets
Exhibit No.___(TJK-6)
FPL Historical Storm Damage Comparisons

Storm Damage per SPH-1 Page 23 of 44 (Table 6-1)

Storm Year	Andrew 1992	Erin 1995	Floyd 1999	Georges 1998	Gordon 1994	Irene 1999	All
Model Losses - Transmission	$59,793,270	$495,539	$58,162	$83,098	$67,617	$2,196,226	$62,693,912
Model Losses - Distribution	$378,496,112	$9,006,142	$8,315,153	$9,073,910	$6,031,159	$54,399,910	$465,322,386
Total Model Losses	$438,289,382	$9,501,681	$8,373,315	$9,157,008	$6,098,776	$56,596,136	$528,016,298
FPL Actual Losses	$283,580,000	$6,000,000	$11,200,000	$11,500,000	$5,100,000	$55,000,000	$372,380,000
FPL Losses in $1999	$438,872,215	$8,027,733	$11,200,000	$12,368,250	$7,338,753	$55,000,000	$532,806,951
Difference	-$582,833	$1,473,948	-$2,826,685	-$3,211,242	-$1,239,977	$1,596,136	**-$4,790,653**
Relative Difference	-0.13%	18.36%	-25.24%	-25.96%	-16.90%	2.90%	-0.90%
Actual Cost Escalation Rate	6.44%	7.55%		7.55%	7.55%		

Table 6-1 Restated Utilizing Stated Growth Rate of 4.00%

Storm Year	Andrew 1992	Erin 1995	Floyd 1999	Georges 1998	Gordon 1994	Irene 1999	All
Model Losses - Transmission	$59,793,270	$495,539	$58,162	$83,098	$67,617	$2,196,226	$62,693,912
Model Losses - Distribution	$378,496,112	$9,006,142	$8,315,153	$9,073,910	$6,031,159	$54,399,910	$465,322,386
Total Model Losses	$438,289,382	$9,501,681	$8,373,315	$9,157,008	$6,098,776	$56,596,136	$528,016,298
FPL Actual Losses	$283,580,000	$6,000,000	$11,200,000	$11,500,000	$5,100,000	$55,000,000	$372,380,000
FPL Losses in $1999	$373,171,934	$7,019,151	$11,200,000	$11,960,000	$6,204,930	$55,000,000	$464,556,015
Difference	$65,117,448	$2,482,530	-$2,826,685	-$2,802,992	-$106,154	$1,596,136	**$63,460,283**
Relative Difference	17.45%	35.37%	-25.24%	-23.44%	-1.71%	2.90%	13.66%
Actual Cost Escalation Rate	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%	

Table 6-1 Restated Utilizing Handy-Whitman Escalators

Storm Year	Andrew 1992	Erin 1995	Floyd 1999	Georges 1998	Gordon 1994	Irene 1999	All
FPL Actual Losses	$283,580,000	$6,000,000	$11,200,000	$11,500,000	$5,100,000	$55,000,000	$372,380,000
Transmission Portion	$38,687,169	$312,917	$77,796	$104,360	$56,544	$2,134,288	$41,373,074
Distribution Portion	$244,892,831	$5,687,083	$11,122,204	$11,395,640	$5,043,456	$52,865,712	$331,006,926
Transmission in 1999$	$48,078,620	$333,324	$77,796	$104,057	$64,648	$2,134,288	$50,792,733
Distribution in 1999$	$281,486,012	$5,965,472	$11,122,204	$11,472,121	$5,522,033	$52,865,712	$368,433,554
FPL Losses in 1999$	$329,564,632	$6,298,796	$11,200,000	$11,576,177	$5,586,681	$55,000,000	$419,226,287
Total Model Losses	$438,289,382	$9,501,681	$8,373,315	$9,157,008	$6,098,776	$56,596,136	$528,016,298
Difference	$108,724,750	$3,202,885	-$2,826,685	-$2,419,169	$512,095	$1,596,136	**$108,790,011**
Relative Difference	32.99%	50.85%	-25.24%	-20.90%	9.17%	2.90%	25.95%
Actual Cost Escalation Rate	2.17%	1.22%		0.66%	1.84%		